STATE OF ILLINOIS ILLINOIS COMMERCE COMMISSION

North Shore Gas Company

Proposed addition of a new service called Rider Purchase of Receivables, (tariffs filed on December 18, 2015)

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Docket No. 16-0033

The Peoples Gas Light and Coke

Company

(Cons)

Proposed addition of a new service

called Rider Purchase of Receivables, (tariffs filed on December 18, 2015)

Docket No. 16-0034

INITIAL BRIEF OF THE STAFF OF THE ILLINOIS COMMERCE COMMISSION

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Table of Contents

			Page
l.	INT	FRODUCTION	1
	A. Procedural Background		1
	B. Relevant Law		4
II.	. ARGUMENT		5
	A. Uncontested Issues		5
	1.	Carrying charge	5
	2.	Rider POR over/under recovery of costs language	6
	3.	Rider UEA Uncollectilbles rider language	7
	B. Contested Issues		8
	1.	The Commission has the authority to approve Rider POR	8
	2.	The Commission should find Rider POR to be just and reasonable	9
	3.	The Commission should not adopt CUB's proposed condition for Rider POR	
III.	CO	NCLUSION	15

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Staff of the Illinois Commerce Commission ("Staff"), by and through its counsel, pursuant to Section 200.800 of the Rules of Practice (83 III. Adm. Code 200.800) of the Illinois Commerce Commission ("Commission"), respectfully submits its Initial Brief ("IB") in the above-captioned matter.

I. INTRODUCTION

A. Procedural Background

On December 18, 2015, North Shore Gas Company ("North Shore") and the Peoples Gas Light and Coke Company ("Peoples Gas") (jointly, "the Utilities" or "the Companies") pursuant to Section 9-201 of the Public Utilities Act ("PUA") each filed various rate schedule sheets ("Filed Rate Schedule Sheets") in which the Companies

Docket Nos. 16-0033/0034 (Cons.) Staff Initial Brief

proposed the addition of a new service under a rider called Rider Purchase of Receivables ("Rider POR"), to be effective February 1, 2016.

On January 20, 2016, the Commission suspended the Filed Rate Schedule Sheets for a period of one hundred and five (105) days. (North Shore, Suspension Order, ICC Docket No. 16-0033, January 20, 2016; Peoples Gas, Suspension Order, ICC Docket No. 16-0034, January 20, 2016.)

On February 9, 2016, an initial status hearing was held at the Commission's Chicago office. The matters were consolidated and a date was set for the filing of the Companies direct testimony. The matter was continued to April 14, 2016. (Tr. 6-10, February 9, 2016.)

On March 22, 2016, the Companies filed the direct testimony of Debra E. Egelhoff, Manager, Gas Regulatory Policy, (NS-PGL Ex. 1.0) and Jerard Julian, Manager of Billing in Customer Relations, (NS-PGL Ex. 2.0).

On April 13, 2016, the status hearing schedule for April 14, 2016 was cancelled and the matter was continued to June 2, 2016 by agreement of the parties. The parties also agreed that Staff and Intervenor direct testimony would be due May 25, 2016. (ALJ Notice, April 13, 2016.)

On May 10, 2016 the Commission re-suspended the Filed Rate Schedule Sheets for six (6) months. The suspension period extends to and includes November 15, 2016. (North Shore, Resuspension Order, ICC Docket No. 16-0033, May 10, 2016; Peoples Gas, Resuspension Order, ICC Docket No. 16-0034, May 10, 2016.)

During the course of the proceeding, the following parties filed appearances and /or intervened in this consolidated matter: Staff, the People of the State of Illinois by Attorney General Lisa Madigan ("AG"), the Citizens Utility Board ("CUB"), the Retail

Energy Supply Association ("RESA"), the Illinois Competitive Energy Association ("ICEA") and Prairie Point Energy, LLC d/b/a Nicor Advanced Energy, LLC ("Nicor Advanced").

On May 25, 2016, Staff filed the direct testimony¹ of David Rearden, Senior Economist (ICC Staff Ex. 1.0), Rochelle M. Phipps, Senior Financial Analyst (ICC Staff Ex. 2.0) and Burma C. Jones, Accountant (ICC Staff Ex. 3.0). CUB filed direct testimony of Bryan McDaniel, Senior Policy Analyst (CUB Ex. 1.0). RESA and ICEA jointly filed the direct testimony of Kevin Wright, President of ICEA².

On June 2, 2016, the parties agreed to a schedule for the remainder of the proceeding. The parties agreed that Staff and Intervenor would file one more round of testimony, cross rebuttal, with the Companies subsequently filing rebuttal testimony. Also, a date for an evidentiary hearings and briefing schedule was set. (Tr. 17-20, June 2, 2016.)

On July 19, 2016, Staff filed the cross rebuttal testimony of David Rearden (ICC Staff Ex. 4.0). CUB filed the rebuttal testimony of Bryan McDaniel (CUB Ex. 2.0). ICEA/RESA filed the rebuttal testimony of Kevin Wright (ICEA/RESA Ex. 2.0).

On August 5, 2016, the Companies filed rebuttal testimony of Debra E. Egelhoff, Manager, Gas Regulatory Policy, (NS-PGL Ex. 3.0).

An evidentiary hearing was held on August 16, 2016, at the Commission's Chicago offices. The testimony and exhibits of Staff, the Companies, CUB and RESA/ICEA were admitted into evidence. (Tr. [], August 16, 2016.) At the conclusion of the evidentiary hearing, the ALJ marked the record heard and taken. (ALJ Ruling, August 16, 2016.)

¹ Revised direct testimony for David Rearden, Staff Ex. 1.0 Rev., was filed on June 1, 2016.

² ICEA/RESA direct testimony for Kevin Wright filed on e-docket on May 25, 2016 is not marked with an exhibit number.

The parties agreed to the filing of simultaneous initial and reply briefs on August 30, 2016 and September 8, 2016, respectively. Staff's IB follows.

B. Relevant Law

Section 9-201 of the PUA is the relevant section of the PUA at issue in this proceeding. Section 9-201 provides in relevant part that:

(c) If the Commission enters upon a hearing concerning the propriety of any proposed rate or other charge, classification, contract, practice, rule or regulation, the Commission shall establish the rates or other charges, classifications, contracts, practices, rules or regulations proposed, in whole or in part, or others in lieu thereof, which it shall find to be just and reasonable. In such hearing, the burden of proof to establish the justness and reasonableness of the proposed rates or other charges, classifications, contracts, practices, rules or regulations, in whole and in part, shall be upon the utility. The utility, the staff of the Commission, the Attorney General, or any party to a proceeding initiated under this Section who has been granted intervenor status and submitted a post-hearing brief must be given the opportunity to present oral argument, if requested no later than the date for filing exceptions, on the propriety of any proposed rate or other charge, classification, contract, practice, rule, or regulation. No rate or other charge, classification, contract, practice, rule or regulation shall be found just and reasonable unless it is consistent with Sections of this Article.

(220 ILCS 5/9-201(c))(emphasis added) Accordingly, the burden of proof is on the Companies to establish the just and reasonableness of Rider POR. (220 ILCS 5/9-201). A "just and reasonable rate" is necessarily a question of sound business judgment, rather than one of legal formula. State Public Utilities Comm'n v. Springfield Gas & Electric Co., 291 III. 209, 218 (1919). "Like so many other questions in the law that involve reasonableness of conduct, it is a question of fact to be settled by the good sense of the tribunal it may come before." Id. The Commission in its final order for Northern Illinois Gas Company's purchase of receivables rider stated that Illinois courts have held that to reach a just and reasonable determination, the Commission must analyze the impact on

consumers. See Abbott Laboratories v. Illinois Commerce Comm'n, 682 NE2d 340, 350 (III. App. Ct. 1st Dist. 1997; Citizens Utility Board v. Illinois Commerce Comm'n, 658 N.E.2d 1194, 1201 (III. App. Ct. 1st Dist. 1995) (Northern Illinois Gas Company, ICC Order Docket No. 12-0569, 18, (July 29, 2013.). The Companies have the burden to prove this by a preponderance of the evidence. (5 ILCS 100/10-15). Preponderance of the evidence has been defined as proof that makes the condition more probable than not. (See, e.g., In re N.B., 191 III.2d at 338, 343 (2000)).

II. ARGUMENT

A. Uncontested Issues³

1. Carrying charge

Under proposed Rider POR, the Utilities would recover exclusively from POR suppliers the capital costs associated with implementing Rider POR plus a carrying charge based on a rate that equals the Utilities' most recent Commission-authorized rate of return on rate base (i.e., the "POR assets"). Under the Utilities' proposal, the POR assets would be recovered exclusively from POR suppliers through a rider with a reconciliation mechanism, meaning retail customers would neither directly nor indirectly guarantee recovery of the POR assets. Staff witness Phipps had no objection to the Utilities' proposal. (Staff Ex. 2.0, 2.)

Staff witness Phipps explained in her testimony that if Rider POR was changed in a manner that would permit the Utilities to recover any portion of POR assets from retail

³ Assuming the Commission finds Rider POR to be just and reasonable, which it should, it is Staff's belief that the issues listed below are uncontested.

customers through a rider with a reconciliation mechanism, then she would recommend the Commission reflect a lower rate of return in the calculation of the POR assets than the overall rate of return last authorized by the Commission for the Utilities' rate base assets. In her judgment, POR assets recovered through a rider with a reconciliation mechanism are less risky than rate base assets and, thus, warrant a lower rate of return than rate base assets. (Id.) She noted that the Commission has endorsed this principle when retail customers have effectively guaranteed the recovery of assets through rider mechanisms that ensure dollar for dollar cost recovery for a public utility – e.g. see Order, Docket No. 10-0138, Commonwealth Edison Company Proposal to Establish Rider PORCB (Purchase of Receivables with Consolidated Billing), Dec. 15, 2010, 40, 47. (Id.)

Staff recognizes that the carrying charge applicable to the capital costs associated with implementing Rider POR is an uncontested issue in this case and, thus, need not be addressed by a finding in the Commission's final order. However, Staff recommends the Commission's final order include the following language where it sets forth Staff's position in this case:

Staff does not object to the carrying charge the Utilities propose to use in the POR Application Charge because the Utilities propose to recover the POR assets exclusively from alternative gas suppliers that voluntarily participate in the POR program. Staff explained that if the Utilities proposal required retail customers to guarantee obligations of those participating suppliers, then Staff would recommend a reduction to the carrying charge that reflects the lower risk and shorter recovery period for POR assets in comparison to rate base assets.

2. Rider POR over/under recovery of costs language

Staff witness Burma Jones proposed the addition of language to Rider POR to clarify to whom the Utilities will refund/charge the over/under-collected amount from the reconciliation called for by Rider POR. Ms. Jones proposed that language be included

that specifies that the over/under-collected amount would be refunded/charged to the participating POR suppliers. (ICC Staff Ex. 3.0, 2-4.) The specific language change proposed by Ms. Jones to Section F of Rider POR is the underlined portion of the following:

Within three months of the end of the recovery period, the Company will reconcile the investment costs with the amounts billed to the participating POR Suppliers <u>and refund to or charge participating POR Suppliers any difference.</u>

The Utilities have no objection to Ms. Jones proposal. (<u>Id</u>.) ICEA/RESA had no objections as well (ICEA/RESA Ex. 2.0, 2.) and CUB did not address the proposal in its rebuttal testimony. Accordingly, it is Staff's belief that this issue is uncontested.

3. Rider UEA Uncollectilbles rider language

Staff witness Burma Jones recommended that Section F(2) of Rider UEA, to which the Utilities proposed changes in conjunction with their Rider POR filling, should include a definition of the RA factor.⁴ (ICC Staff Ex. 3.0, 5.) In response to a Staff data request, the Utilities indicated the omission of a definition for the RA factor was inadvertent. Staff witness Jones had no objection to the following definition proposed by the Utilities, which mirrors the definition for the RA factor used elsewhere in Rider UEA. (Id.):

RAc = Reconciliation Adjustment, in dollars, which shall be determined annually for each service classification by subtracting actual booked ISUA revenues from expected ISUA revenues. Expected ISUA revenues shall be calculated based upon the previous effective period's ISUA adjustment multiplied by forecasted number of gas supply service customer billing periods as filed for the prior June 1 through May 31 period. The reconciliation component shall be collected over 9 months, from September through May, and shall be supported by a Commission filing made annually on

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⁴ RA refers to reconciliation adjustment.

or before August 31. No reconciliation component shall be included in the June through August period.

ICEA/RESA had no objections to the proposal (ICEA/RESA Ex. 2.0, 2.) and CUB did not address the proposal in its rebuttal testimony. Accordingly, it is Staff's belief that this issue is uncontested.

B. Contested Issues⁵

1. The Commission has the authority to approve Rider POR

The Commission has the authority to approve Rider POR. CUB witness McDaniel testified that "[w]hile I am not an attorney, I do not believe the Commission is specifically authorized by statute, nor is it obligated to approve a POR tariff for gas utilities." (CUB Ex. 1.0, L 70-71.) It is not exactly clear what CUB intends by these statements. With regard to the statement that there is no obligation to approve Rider POR, Staff would agree that just because certain parties entered into a settlement agreement which provided that North Shore and Peoples Gas would file a tariff and seek Commission approval of a purchase of receivables program, the Commission is not obligated to approve the rider. However, with regard to CUB's statement that the purchase of receivables rider is not specifically authorized by statute, the meaning of that statement is vague. It is true that for alternative gas suppliers ("AGS") there is no section 16-118(c) like there is for Alternative Retail Electric suppliers ("ARES"), however, Section 9-201 of the PUA gives the Commission broad authority to approve tariff changes, if they are just and reasonable. Therefore, the Commission can approve Rider POR if the Commission

⁵ The following issues are those that Staff believes are contested in this proceeding. That belief is based upon the testimony filed by the Companies and Intervenors. With respect to the first contested issue, it is not clear from CUB's testimony if CUB is contesting the Commission's authority to approve Rider POR.

finds it just and reasonable. The Commission addressed this issue in Docket No. 12-0659⁶. The Commission stated in part the following:

CUB/AG argue that the Commission lacks legal authority to approve Rider 17. Specifically, CUB/AG argue that, absent specific statutory authority, the Commission cannot approve a PORCB program. The Commission disagrees. As noted by Nicor in its Reply Brief, the Commission has broad authority to set and design utility rates, and included within that authority is the ability to approve riders as a preferred mechanism for cost recovery. See Business and Prof'l People for the Pub. Interest v. Illinois Commerce Comm'n. 136 III. 2d 192, 204 (1989) ("BPI"); Citizens Utility Bd. V. Illinois Commerce Comm'n, 166 III. 2d 111, 140 (1995). The Commission exercised such authority in approving Rider 15 - Customer Select Program, which was filed pursuant to Section 9-201 of the Act. Nicor filed Rider 17 pursuant to the same statutory provision.

(Northern Illinois Gas Company, ICC Order Docket No. 12-0569, 17, (July 29, 2013.). Consistent with the Commission's order in Docket No. 12-0569, the Commission should find that it has the authority to approve Rider POR, if its finds it just and reasonable, which it should, for the reasons set forth below.

2. The Commission should find Rider POR to be just and reasonable

Staff does not oppose Rider POR nor the modifications to the other tariffs. Dr. Rearden provided three reasons for this position. One, it does not assess any charges on sales customers. Sales customers will not take service under Rider POR. Two, it does not seem likely that it will raise prices in the retail market above what they would have been absent a Rider POR. Three, the design of the tariff is appropriate, and the risk that Peoples Gas and North Shore could earn revenues above costs is small. (Staff Ex. 1.0 (Rev.), 3:54-59.)

⁶ Docket No. 12-0569 involved a tariff proposal by Northern Illinois Gas Company to offer purcha se of receivables and consolidated billing.

In its proposed Rider POR, the Utilities recover the cost to implement POR by requiring that an AGS wishing to use the service commit to paying the incremental costs. A participating AGS must pay its share of those costs amortized over a five-year period. The proposed tariff requires any AGS that wants to use the service to provide an irrevocable standby letter of credit to the Utilities for its share of the costs to develop the service before the service begins.⁷ Ratepayers are thus insulated from directly paying for the service. (Id., 3:614:67.)

The discount rate used for a receivable purchased under Rider POR is initially set at the Uncollectible Factors defined in Rider UEA-GC. However, 36 months after the rider begins, the Utilities will revise the POR uncollectible rate for each Service Classification based upon the Utilities experience with POR customers' uncollectibles. In this way, there will be separate discount rates for sales and transportation customers. Thus, sales customers are insulated from any effects that the POR transportation customers might have on the uncollectibles rate. (Id., 4:69-77.)

CUB witness Mr. McDaniel complains that Rider POR could raise the overall uncollectibles rate, harming sales customers. This concern is unwarranted. At the start, the Utilities propose to use the existing discount factor for Rider POR customers for each classification. Thus, the discount factor is fixed for the initial period and does not depend upon the uncollectibles that actually occur. After 36 months, the discount factors will be set "for each Service Classification using data underlying the participating suppliers' customers' net write-off amounts." (NSG-PGL Ex. 1.0, 10:206-207) Therefore,

⁷ If an AGS decides to take service under Rider POR after the service is implemented, it will similarly need to assure the Utilities that it will pay its share of the costs.

the suppliers as a group will not have an incentive to market more intensively to customers with histories of nonpayment, since nonpayment will be reflected in the discount rates that suppliers will eventually face. (Staff Ex. 4.0, 3:44-54.)

In analyzing the effect of Rider POR on retail gas prices, the comparison should be between the price with and without a purchase of receivables. That comparison depends on two factors: the effect that Rider POR has on AGS costs and the competitiveness of the retail market. If Rider POR lowers AGS costs, then retail prices should fall relative to the price that would result if there is no Rider POR. (Staff 1.0 (Rev.), 4:81-5:87.) Dr. Rearden testified that it was reasonable to believe that a tariff like Rider POR will provide bill collection services at lower cost than if the suppliers collect their own bills. In particular, suppliers have argued that under a tariff like Rider POR, the utility has better leverage to collect bills, since, unlike an AGS, it can shut off service when the bill is not paid. (Id., 5:89-94.) Dr. Rearden testified that the market appears to be relatively competitive. Suppliers can relatively easily enter and exit the market, which is one indicator of a functionally competitive market. It seems reasonable to conclude that, even in the short term, lower costs are likely to be passed on to consumers. (Id., 5:98-101.)

CUB witness Mr. McDaniel, on the other hand, asserts that the tariff has not been shown to provide benefits to customers nor that it has been shown to be just and reasonable. Rather than address the question of whether POR provides benefits or is cost justified, Mr. McDaniel focuses instead on costs and benefits of small volume transportation services ("SVT"). Therefore, in order for CUB's argument to be valid, either Rider POR must raise prices, or marketers will market products with the same high prices to more unwitting customers. Dr. Rearden testified that it is likely instead that Rider POR will lower AGS costs, and as long as the demand curve slopes downward, i.e., the quantity

demanded increases when price decreases, a cost decrease leads to a price decrease. The degree to which the market responds to lower costs with lower prices depends upon the shape of the market demand curve. If it is flat, then prices will not fall very far, while a steeper demand curve implies a larger price decrease. The conclusion that lower costs leads to lower prices holds even if the market is a monopoly. The single firm has the incentive to maximize profits by lowering price and increasing quantity, as long as the market demand curve is downward sloping. (Staff Ex. 4.0, 5:99-6:118.)

Further, Dr. Rearden opined that the net benefits issue is irrelevant, since its costs are not socialized with all other customers. Suppliers pay all the startup costs for the service, so whether it is worth its costs does not affect the costs borne at all by sales customers or directly by transportation customers. (Id., 6:119-124.)

CUB witness Mr. McDaniel worries that "POR Suppliers could target neighborhoods with large numbers of high credit risk customers" or "potential customers who are having trouble paying their bills." (CUB Ex. 1.0, 97-103) Staff witness Dr. Rearden noted that participating suppliers have an incentive to keep uncollectibles low in order to benefit from a lower Rider POR discount rate in the future. Further, even though an individual supplier with a customer base that consists of relatively higher credit risk customers faces the same discount rate as all other suppliers, such a supplier only benefits from that discount rate to the extent that it can charge higher prices to high risk customers. Thus the incentive to "target" such neighborhoods only exists if those customers pay higher prices. (Id., 3:55-4:67.)

CUB witness Mr. McDaniel also suggests Rider POR could drain the Low Income Home Energy Assistance Program ("LIHEAP") fund faster. His argument is that higher prices commonly mean higher bills, so greater LIHEAP payments are required to continue service for lower income households. However, as noted above, it does not appear likely that Rider POR will force prices higher. Therefore, Dr. Rearden argues that while such an outcome is a theoretical possibility in the short run, a general conclusion regarding the effect of making transportation service available to LIHEAP-eligible customers requires knowledge about how far prices fall and how responsive quantity demanded by LIHEAP-eligible customers is to price in the transportation market. In particular, the farther the price drops and the fewer LIHEAP-eligible customers switch to transportation service, the less likely it is that the LIHEAP fund is pressured. However, it is difficult to reach a definitive conclusion without more information. Staff recommends that if the Commission is concerned that LIHEAP is threatened, it could direct Staff to monitor the market for its effects on LIHEAP. If the fund is pressured, the Commission Staff can consider alternatives to bring to the Commission at that time to address any pressuring of the fund. (Id., 4:68-5:92.)

Finally, in response to CUB witness Mr. McDaniel's concern about the effect on low income neighborhoods, Staff witness Dr. Rearden suggested that since the Utilities are going to collect the bills for all participating suppliers, it will have information on the total bill amounts and volumes for each participating customer. That information could be used to compare AGS prices to the rates that sales customers pay, and whether some customers pay systematically higher prices. That comparison could be made in aggregate for all suppliers and for each individual supplier. The comparison could be made each month, over several months, or a year. A sample could be drawn of individual

⁸ Similarly, the less the price drops and the more LIHEAP customers switch to transportation ser vice, the more likely it that the LIHEAP fund is pressured.

customers to examine their results, which would allow the Commission to examine a range of outcomes that might highlight the best offers. Of course, precautions would need to be taken to protect confidential and competitively sensitive information. The data could either be made anonymous or sufficiently aggregated to preclude those concerns. (Id., 9:178-10:194.)

3. The Commission should not adopt CUB's proposed condition for Rider POR

While CUB opposes Rider POR and recommends that it be rejected, CUB proposed a condition in the event the Commission is inclined to approve Rider POR. (CUB Ex. 1.0, lines 197-203) CUB witness Mr. McDaniel's proposed condition is that suppliers be limited in the amount that can be recovered through Rider POR. In particular, the utility could only buy receivables each month equal to the amount that would have been billed at the PGA price. (CUB Ex. 1.0, 177-195) Staff notes that there are several difficulties associated with this proposal. First, the restriction is asymmetric. For some offers during some months, the unregulated price could be below the PGA rate; during other months for the same offer, the opposite could be true, due to fluctuations in the PGA. In the latter case, the supplier is punished by PGA fluctuations, which are not directly tied to current prices. Second, it requires suppliers to send separate bills to its customers in some, but not all, circumstances, reducing the single-bill benefits of POR. Third, the administrative complications, such as notifications when the supplier needs to send a separate bill and determining how much that bill should be, might make the proposal unworkable by itself. Fourth, it re-introduces uncertainty into how suppliers formulate their prices, negating that benefit for customers and suppliers. In sum, Mr.

Docket Nos. 16-0033/0034 (Cons.) Staff Initial Brief

McDaniel's proposed condition undermines the very advantages that POR is otherwise intended to provide and therefore should be rejected. (Id., 7:140-8:157.)

III. CONCLUSION

Staff respectfully requests that the Illinois Commerce Commission approve Staff's recommendations in this docket.

Respectfully submitted,

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